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In the Supreme Court of the United States

OCTOBER TERM, 1948

No. 645

UNIVERSAL ATLAS CEMENT COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court of the United States (R. 42-49) [1] is reported in 9 T.C. 971. The *per curiam* opinion of the Court of Appeals (R. 72) is reported in 171 F. 2d 294.

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[1] The record references are to the Petitioner's Appendix, the Respondent's Appendix and the Proceedings in the Court of Appeals for the Second Circuit unless otherwise indicated. A duplicate certified copy of the Transcript of Record has been filed with the Clerk of this Court.

JURISDICTION

The judgment of the Court of Appeals was entered on December 17, 1948. (R. 72-73.) The petition for a writ of certiorari was filed on March 15, 1949. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether the sum of $100,000 paid by the taxpayer in 1939 in compromise of an anti-trust suit brought against it by the State of Texas was deductible from gross income as an "ordinary and necessary" business expense within the meaning of Section 23 (a)(1)(A) of the Internal Revenue Code, as amended.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) [As amended by Section 121 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798][2]

Expenses.—

(1) *Trade or business expenses.*—

(A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business * * *

* * * * *

[2] This amendment was made applicable to taxable years beginning after December 31, 1938, by Section 121 (d) of the Revenue Act of 1942.

(26 U.S.C. 1946 ed., Sec. 23.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

> SEC. 19.23 (a)-1. *Business Expenses.*—Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except the classes of items which are deductible under sections 23 (b) to 23 (s), inclusive, and the regulations thereunder. Double deductions are not permitted. Amounts deducted under one provision of the Internal Revenue Code cannot again be deducted under any other provision thereof. * * *. Penalty payments with respect to Federal taxes, whether on account of negligence, delinquency, or fraud, are not deductible from gross income. * * *.

STATEMENT

The stipulation of facts (R. 9-11) and the exhibits attached to it were adopted by the Tax Court (R. 43). The facts as found by the Tax Court (R. 43-46) may be summarized as follows:

Prior to and during 1939, the taxable year, the taxpayer was engaged in the business of manufacturing and selling cement in various parts of the United States, including Texas. On March 7, 1938, the State of Texas filed a suit against the taxpayer and five other companies (including Longhorn Portland Cement Company), alleging that they had entered into a conspiracy to violate the anti-trust laws of the State of Texas and had

committed various acts in connection with the conspiracy, and praying for penalties, forfeitures, etc., as provided by Articles 7426 through 7447, 20 Vernon's Texas Civil Statutes Annotated (1925). (R. 43.) Later the State of Texas filed an amended petition against the taxpayer and those other corporations incorporated outside the State of Texas which charged the defendants with conspiracy in various ways to restrain trade, to fix the price of cement and to prevent and lessen competition. (R. 43-44.)[3] The petition sought to impose penalties of from $50 to $1,500 per day from 1930 until 1938, to impose a lien for the penalties on all of the properties of the defendants, to cancel the permits of the defendants to do business in Texas, to have a receiver appointed, and for an injunction. (R. 44.)

After a series of hearings in the nature of pretrial examinations had been held over a period of six months, a settlement agreement was entered into whereby the four defendants, including the taxpayer, paid $400,000 in full satisfaction of all claims for penalties. (R. 44.) The Court entered its decree,[4] pursuant to which the taxpayer paid the State of Texas $100,000 as its share of the $400,000, provided for in the agreement. The taxpayer deducted the sum so paid on its federal in-

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[3] The taxpayer in this case was also a defendant in proceedings brought by the Federal Trade Commission. See *Trade Comm'n* v. *Cement Institute*, 333 U. S. 683.

[4] The final decree, including the settlement agreement, constitutes Exhibit E, attached to the Stipulation of Facts. (R. 52-70.)

come tax return for 1939, but the Commissioner disallowed the deduction. (R. 46.) The Tax Court, with two judges dissenting, upheld the Commissioner (R. 49), and the court below, in a *per curiam* opinion, affirmed the decision of the Tax Court (R. 72).

ARGUMENT

1. This case is substantially identical with *Commissioner* v. *Longhorn Portland Cem. Co.*, 148 F. 2d 276 (C.A. 5), in which this Court denied certiorari, 326 U. S. 728. There is no more reason for further review in this case. The Longhorn Company was one of the defendants in the original action brought against the taxpayer in this case. (R. 9, 43.) Subsequently, a separate action was brought by the State of Texas against the Longhorn Company and another corporation, both of which were incorporated in Texas, for violation of the anti-trust laws, in which the State sought to recover statutory penalties and other affirmative relief. Each corporation paid the State in 1939 the sum of $50,000 in compromise of the suit, and an agreed judgment was entered, just as in this case, which recited that the payments were in full satisfaction of all claims of the State for penalties for the alleged violations of law, but that the defendants did not thereby admit, or estop themselves to deny, the truth of the allegations of the petition. The corporations sought to deduct the sums in question as ordinary and necessary business expenses and the Tax Court permitted them to take the deductions on the ground that the compromise payments were not

penal in nature. On appeal, the Fifth Circuit reversed the decision of the Tax Court and held that the sums in question were paid as penalties and therefore were not deductible.

The court below affirmed the decision of the Tax Court in the present case on the authority of the *Longhorn Portland Cem. Co.* case. (R. 72.) See also *Helvering* v. *Superior Wines & Liquors,* 134 F. 2d 373 (C.A. 8th); *United States* v. *Jaffray,* 97 F. 2d 488 (C.A. 8th), affirmed on other grounds, 306 U. S. 276; *Standard Oil Co.* v. *Commissioner,* 129 F. 2d 363 (C.A. 7th), certiorari denied, 317 U. S. 688; Treasury Regulations 103, Sec. 19.23 (a)-1, *supra.*[5]

In *Commissioner* v. *Heininger,* 320 U. S. 467, involving the deduction of attorney's fees in a Post Office fraud order case, this Court said (p. 473):

> Where a taxpayer has violated a federal or a state statute and incurred a fine or penalty he has not been permitted a tax deduction for its payment.

An action under the Texas anti-trust act has been held penal in nature. See *Waters-Pierce Oil Co.* v. *State of Texas,* 48 Tex. Civ. App. 162, 181, writ

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[5] Compare *Commissioner* v. *Heide,* 165 F. 2d 699 (C.A. 2d), and *Commissioner* v. *Josephs,* 168 F. 2d 233 (C.A. 8th), certiorari denied, 335 U. S. 871, in both of which cases an amount paid in compromise of a civil suit based on negligence was not allowed as a deduction as an ordinary and necessary expense under Section 23 (a) (2) of the Internal Revenue Code, dealing with non-business expenses.

of error refused, 103 Tex. 676, affirmed, 212 U. S. 86. While there was a compromise in the present case, the decree expressly states that the sum in question was paid in full satisfaction of all penalties for alleged violations of the Texas statute. (R. 69.) The compromise, therefore, has the same effect as though there had been a conviction after a trial upon the merits. *United States* v. *Chouteau*, 102 U. S. 603, 611.

The petition for certiorari describes at length the motives which led the taxpayer to compromise the suit by the State of Texas for violation of its anti-trust laws. (Pet. 6-8.) But the motives of the taxpayer are unimportant in a case of this kind; the only question is whether the amount paid in compromise was a penalty, or resembles a penalty so closely that it should be treated as one. Although the settlement agreement recites that it was not an admission by the taxpayer of guilt (R. 66-67), the judgment speaks for itself.

The taxpayer argues that the decision of the court below puts a premium on continuing anti-trust litigation. (Pet. 11.) But if the taxpayer had continued to contest the suit and had then been found guilty, the penalties might have amounted to $200,000 or $300,000 instead of $100,000. A defendant in an anti-trust case may find it profitable to compromise, regardless of tax effect. It may be pointed out that the taxpayer here was allowed to deduct the expenses of the litigation, just as the

taxpayer in *Commissioner* v. *Heininger,* 320 U. S. 467, was allowed to deduct them; it is only a penalty that may not be deducted.

2. There is no conflict of decisions. While the taxpayer alleges that the decision of the court below is in conflict with the decisions of this Court in *Commissioner* v. *Heininger, supra; Welch* v. *Helvering,* 290 U. S. 111; and *Kornhauser* v. *United States,* 276 U. S. 145 (Pet. 6), none of these cases involved the deduction of penalties or amounts paid in compromise of a suit for penalties.

CONCLUSION

The decision of the court below is correct. There is no conflict of decisions. The petition for a writ of certiorari should be denied.

Respectfully submitted,

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APRIL, 1949.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1949 832003